

Message Text

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ACTION EB-08

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FM AMEMBASSY MANAGUA
TO SECSTATE WASHDC 5786
INFO AMEMBASSY GUATEMALA
AMEMBASSY SAN JOSE
AMEMBASSY SAN SALVADOR
AMEMBASSY TEGUCIGALPA

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E.O. 11652: N/A
TAGS: EINV, EIND, EFIN, NU
SUBJECT: UPDATE OF INVESTMENT CLIMATE STATEMENT

REF: A) 77 STATE 244738, B) MANAGUA 0490 (NOTAL)

BEGIN SUMMARY: THE LEGAL STRUCTURE FOR FOREIGN INVESTMENT IN NICARAGUA IS EXCELLENT. THERE ARE NO RESTRICTIONS ON THE REPATRIATION OF PROFITS AND DIVIDENDS, AND FOREIGN CITIZENS AND CORPORATIONS ARE ENSURED TREATMENT EQUAL TO THAT ACCORDED TO NICARAGUAN CORPORATIONS AND CITIZENS. FOREIGN NATIONALS MAY OWN CORPORATIONS IN ANY SECTOR OF THE ECONOMY. IN GENERAL THE GOVERNMENT OF NICARAGUA (GON) ENCOURAGES FOREIGN INVESTMENT AND THE EMBASSY KNOWS OF NO MAJOR CASES OF DISCRIMINATION AGAINST AMERICAN INVESTORS. THE CENTRAL BANK OF NICARAGUA ESTIMATES THAT TOTAL DIRECT FOREIGN INVESTMENT IN THE COUNTRY EQUALS \$320 MILLION, FIFTY PERCENT OF WHICH WAS U.S. GENERATED. THE POLITICAL STABILITY WHICH NICARAGUA HAS ENJOYED OVER THE PAST FOUR DECADES WAS SHAKEN IN 1977 BY A SERIES OF EVENTS WHICH CULMINATED IN A TWO-WEEK GENERAL WORK STOPPAGE WHICH ENDED IN FEBRUARY 1978. POTENTIAL INVESTORS SHOULD ALSO BE AWARE OF CURRENT ECONOMIC ISSUES

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SUCH AS THE NON-AVAILABILITY OF INEXPENSIVE AND RELIABLE ELECTRIC POWER, LIMITED LIQUIDITY IN THE FINANCIAL SECTOR, AND ALLEGATIONS OF CORRUPTION. ALTHOUGH NICARAGUA, IN THE AGGREGATE VIEW, OFFERS PROMISING OPPORTUNITIES TO THE FOREIGN INVESTOR, BUSINESSMEN ARE URGED TO UNDERTAKE A THOROUGH INVESTIGATION BEFORE MAKING A FINAL INVESTMENT DECISION. END SUMMARY

1. THE LEGAL STRUCTURE:

A. THE LEGAL STRUCTURE FOR FOREIGN INVESTMENT IN NICARAGUA IS EXCELLENT. UNDER THE FOREIGN INVESTMENT LAW OF 1955, THERE ARE NO RESTRICTIONS ON THE REPATRIATION OF PROFITS, DIVIDENDS, ETC. AND FOREIGN CAPITAL MAY ENTER AND LEAVE NICARAGUA WITHOUT RESTRICTION. THE TREATY OF FRIENDSHIP, COMMERCE, AND NAVIGATION OF 1956 BETWEEN THE U.S. AND NICARAGUA ENSURES THAT CITIZENS AND CORPORATIONS OF THE U.S. RECEIVE TREATMENT NO LESS FAVORABLE THAN THAT ACCORDED LOCAL CITIZENS AND CORPORATIONS. EXPROPRIATION CAN BE UNDERTAKEN ONLY IN CASES OF PUBLIC INTEREST AND WITH PROMPT AND JUST COMPENSATION. AS A MEMBER OF THE CENTRAL AMERICAN COMMON MARKET (CACM), NICARAGUA ADHERES TO CENTRAL AMERICAN AGREEMENT ON FISCAL INCENTIVES TO INDUSTRIAL DEVELOPMENT. (OTHER MEMBERS OF THE CACM ARE COSTA RICA, HONDURAS, EL SALVADOR, AND GUATEMALA.) THE INCENTIVES, WHICH ARE UNIFORM, THROUGHOUT THE CACM, ARE AWARDED ON A SLIDING SCALE ACCORDING TO THE CLASSIFICATION AWARDED A COMPANY BY THE NICARAGUAN MINISTRY OF ECONOMY. ELIGIBLE FOR BENEFITS ARE THOSE INDUSTRIES WHICH USE MODERN AND EFFICIENT METHODS OF PROCESSING RAW MATERIAL AND SEMIFINISHED PRODUCTS, WHICH PRODUCE ARTICLES NECESSARY FOR OTHER PRODUCTIVE INDUSTRIES, WHICH SATISFY BASIC NEEDS OF THE POPULATION, WHICH REPLACE ARTICLES BEING IMPORTED IN CONSIDERABLE QUANTITY, OR WHICH INCREASE THE VOLUME OF EXPORTS.

B. OTHER PERTINENT LAWS INCLUDE INCENTIVES GRANTED TO INDUSTRIAL PLANTS LOCATED IN THE FREE TRADE ZONE NEAR MANAGUA'S LA MERCEDES AIRPORT. VARIOUS IMPORT DUTY EXEMPTIONS AND TAX ADVANTAGES ARE GRANTED TO FIRMS WHICH ARE ESTABLISHED TO PRODUCE ARTICLES SOLELY FOR EX-UNCLASSIFIED

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PART OUTSIDE THE CACM. TO PROMOTE FOREIGN TOURISM, THERE IS A TOURISM LAW WHICH IS DESIGNED TO ENCOURAGE INVESTMENT IN HOTELS AND ENTERTAINMENT CENTERS. CERTAIN TAX EXEMPTIONS AND DUTY FREE IMPORT ALLOWANCES ARE GRANTED TO INVESTMENT PROJECTS IN THIS SECTOR VALUED AT MORE THAN \$140,000. IN 1977 AN OFFSHORE BANKING LAW WAS PASSED WHICH GRANTS TAX EXEMPTIONS TO BANKS AND FOREIGN FINANCIAL INSTITUTIONS WHICH DEAL EXCLUSIVELY WITH INTERNATIONAL OPERATIONS INVOLVING PERSONS DOMICILED OUTSIDE NICARAGUA. THERE ARE NO SIGNIFICANT LEGAL BARRIERS AFFECTING THE TRANSFER OF TECHNOLOGY AS REGARDS PATENT LAWS, ROYALTY POLICY, ETC.

C. THERE ARE NO REQUIREMENTS FOR LOCAL PARTICIPATION IN FOREIGN-OWNED CORPORATIONS AND, INDEED, FOREIGN NATIONAL CAN HAVE COMPLETE OWNERSHIP OF A FIRM IN ANY SECTOR OF THE ECONOMY. THERE ARE NO RESTRICTIONS ON MOST FOREIGN NATIONALS RESIDING AND WORKING IN NICARAGUA.

2. GON ATTITUDE:

A. IN GENERAL, THE GON ENCOURAGES FOREIGN INVESTMENT AND THE EMBASSY IS NOT AWARE OF ANY MAJOR CASE IN WHICH AMCITS WERE DISCRIMINATED AGAINST UNDER THE LAW. ONE AMERICAN COUPLE, HOWEVER, DID ENCOUNTER DIFFICULTY IN OBTAINING PERMISSION TO IMPORT HOTEL SUPPLIES FOR A SMALL FAMILY-STYLE HOTEL UNDER THE TOURISM LAW, BUT SUBSEQUENTLY

DECIDED NOT TO PROCEED WITH THE PROJECT. ON THE OTHER HAND, LARGE SCALE HOTEL PROJECTS, SOME OF WHICH ARE AFFILIATED WITH US CHAINS, HAVE NOT, TO OUR KNOWLEDGE, ENCOUNTERED LEGAL IMPEDIMENTS. ONE US FIRM COMPLAINED OF AN ADVERSE LABOR COURT DECISION ON A CONTRACT MATTER INVOLVING ACTIONS WHICH THE FIRM HAD TAKEN IN ANOTHER COUNTRY AGAINST A NICARAGUAN EMPLOYEE. THAT EMPLOYEE SUCCESSFULLY BROUGHT SUIT AGAINST THE US FIRM IN A LOCAL COURT EVEN THOUGH THE US FIRM WAS NOT DIRECTLY REPRESENTED IN NICARAGUA. ANOTHER US FIRM EXPERIENCED DIFFICULTY IN IMPORTING EQUIPMENT AND MATERIALS IT MADE FOR ITS INDUSTRIAL OPERATION AND TO WHICH IT FELT ENTITLED UNDER LOCAL INCENTIVE LAW. NONETHELESS, AMERICAN BUSINESSMEN GENERALLY FEEL THAT FROM THE LEGAL STANDPOINT, NICARAGUA IS A VERY GOOD PLACE TO INVEST.

B. THERE HAS BEEN NO PROBLEM, UP UNTIL NOW, WITH REQUESTS FOR OPIC UNCLASSIFIED

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INVESTMENT GUARANTEE PROGRAMS BEING APPROVED BY THE GON.

3. LABOR FACTORS:

LABOR IS GENERALLY AVAILABLE IN NICARAGUA ALTHOUGH THERE MAY BE A SHORTAGE OF UNSKILLED LABOR AT CERTAIN TIMES OF THE YEAR AND THERE IS PERENNIAL LACK OF SKILLED WORKERS. THOUSANDS OF FOREIGN NATIONALS ENTER NICARAGUA EACH YEAR TO HELP WITH COFFEE AND COTTON HARVESTS. ALTHOUGH SKILLED LABOR IN CERTAIN INDUSTRIAL CATEGORIES IS NOT PLENTIFUL, THE MINISTRY OF LABOR HAS VARIOUS PROGRAMS TO UPGRADE THE LEVEL OF SKILLS IN THE LABOR POOL. UNIONS ARE WEAK AND THE

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GON IS GENERALLY PRO-MANAGEMENT. THE PROCEDURE TO INITIATE A LEGAL STRIKE IS VERY COMPLICATED AND IS SELDOM PURSUED. CONSEQUENTLY, THERE HAVE BEEN ONLY THREE OR FOUR LEGAL STRIKES IN THE HISTORY OF NICARAGUA. HOWEVER, ILLEGAL STRIKES DO OCCUR, ESPECIALLY IN THE CONSTRUCTION SECTOR.

4. VALUE OF FOREIGN INVESTMENT:

UNFORETUNATELY, ACCURATE FIGURES FOR U.S. INVESTMENT IN NICARAGUA ARE UNAVAILABLE. SINCE THE CORDOBA IS A FREELY CONVERTIBLE CURRENCY, THE REGISTRATION OF A FOREIGN INVESTMENT WITH THE GON, WHILE ENCOURAGED, IS NOT REQUIRED. THE CENTRAL BANK OF NICARAGUA HAS INDICATED THAT TOTAL REGISTERRED DIRECT FOREIGN INVESTMENT IN NICARAGUA FOR THE YEARS OF 1956 THROUGH 1976 IS \$66 MILLION, EIGHTY PERCENT OF WHICH (\$52.8 MILLION) WAS REGISTERED BY AMERICAN CORPORATIONS OR INDIVIDUALS. (EUROPEAN CORPORATIONS REPRESENTED 4.7 PCT AND JAPANESE ENTITIES 1.2 PCT.) CENTRAL BANK SOURCES ESTIMATE THAT CURRENT TOTAL DIRECT FOREIGN INVESTMENT (I.E., BOTH REGISTERRED AND UNREGISTERED) IS APPROXIMATELY \$320 MILLION, FIFTY PERCENT OF WHCIH (\$160 MILLION) IS U.S.-GENERATED. FIGURES BY SECTOR ARE NOT AVAILABLE.

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5. ECONOMIC AND POLITICAL FACTORS:

NICARAGUA IS AN AGRICULTURE-BASED ECONOMCY OPERATING WITHIN A FREE ENTERPRISE SYSTEM FRAEMEWORK. THE GDP GREW AT A REAL RATE OF 5.5 PCT IN 1977 AND HAS, INDEED, SUSTAINED AN AVERAGE REAL GROWTH RATE OF 5 PCT ANNUALLY OVER THE PAST TWO DECADES. FACTORS CONTRIBUTING TO THE LONG-TERM DEVELOPMENT POTENTIAL OF NICARAGUA ARE ITS NATURAL AGRICULTURAL RESOURCES; THE AVAILABILITY OF A LARGE, RELATIVELY UN-EXPLOITED EASTERN REGION; A RESULTANT LACK OF POPULATION AND UNDEVELOPED HYDROELECTRIC AND GEOTHERMAL ENERGY RESOURCES PRESSURES. NICARAGUA'S ULTIMATE DEVELOPMENT GOAL IS TO CONTINUE ITS GROWTH AS AN AGRICULTURAL ECONOMY AND TO SUPERIMPOSE UPON THIS BASE A DYNAMIC INDUSTRIAL SECTOR WHICH WOULD EMPHASIZE THE ESTABLISHMENT OF AGRO-INDUSTRIES. THE COUNTRY ALSO HAS AN ONGOING PROGRAM TO DEVELOP AND EXPAND NON-TRADITIONAL EXPORTS. HOWEVER, THE SHORT-TERM INVESTMENT PICTURE FOR NICARAGUA IS CLOUDED DUE TO RECENT ECONOMIC AND POLITICAL EVENTS. THESE AND OTHER ISSUES ARE DISCUSSED BELOW:

A. UNTIL MID-1977 NICARAGUA ENJOYED POLITICAL STABILITY UNDER THE RULE OF THE SOMOZA FAMILY WHICH HAS BEEN IN POWER FOR MORE THAN FORTY YEARS. HOWEVER, THIS STABILITY WAS SHAKEN WHEN PRESIDENT SOMOZA SUFFERED A HEART ATTACK IN JULY, GUERRILLA ACTIVITY FLARED IN OCT-OBER, AND VARIOUS GROUPS (INCLUDING THE PRIVATE SECTOR) CALLED FOR GOVERNMENTAL REFORMS. FOLLOWING THE JANUARY 1978 ASSASSINATION OF THE MOST PROMINENT POLITICAL OPPOSITIONIST, CIVIL DEMONSTRATIONS

CAUSED DAMAGE TO A NUMBER OF INDUSTRIAL FIRMS IN MANAGUA. KEY BUSINESS GROUPS THEN JOINED WITH POLITICAL OPPONENTISTS IN CALLING FOR A GENERAL WORK STOPPAGE WHICH LASTED TWO WEEKS. THE STRIKE ENDED IN EARLY FEBRUARY WITHOUT A RESOLUTION OF THE POLITICAL PROBLEMS WHICH PROMPTED THE STRIKE.

B. OVER-LENDING BY THE PRIVATE FINANCIAL SECTOR DURING EARLY 1977, THE SOFTENING OF THE WORLD MARKET PRICES FOR SOME OF NICARAGUA'S LEADING EXPORT EARNERS (I.E. COFFEE AND COTTON), AND WITHDRAWALS OF DEPOSITS FROM FINANCIAL INSTITUTIONS DURING THE RECENT POLITICAL CRISIS HAVE CREATED A SITUATION OF LIMITED LIQUIDITY IN THE FINAN-

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CIAL SECTOR. LOCAL BANKING SOURCES INDICATE THAT THIS ILLIQUIDITY MAY PERSIST THROUGHOUT 1978, THUS MAKING IT MORE DIFFICULT FOR FOREIGN FIRMS WHO WISH TO ESTABLISH THEMSELVES IN NICARAGUA TO OBTAIN LOCAL FIANCING FOR THEIR WORKING CAPITAL NEEDS.

C. ANOTHER ISSUE OF WHICH POTENTIAL INVESTORS SHOULD BE AWARE IS THE COMPLAINT VOICED BY MANY LOCAL AND FOREIGN BUSINESSMEN ABOUT SERIOUS CORRUPTION WITHIN THE PUBLIC SECTOR. HOWEVER, A CABINET RE-ORGANIZATION TOOK PLACE AND DECEMBER AND ALLEGATIONS OF CORRUPTION HAVE ABATED SINCE THEN.

D.

D. ANOTHER POTENTIAL PROBLEM IS THE AVAILABILITY OF INEXPENSIVE AND RELIABLE ELECTRIC POWER. IN 1977, ELECTRICITY HAD TO BE RATIONED DURING THE HEIGHT OF THE DRY SEASON, JANARY-APRIL, WHEN DEMAND WAS AT ITS PEAK, AND THE SPECTRA OF SUCH RATIONING WILL HANG OVER THE ECONOMY DURING FUTURE DRY SEASONS UNTIL ADEQUATE, NEW SOURCES OF POWER COME ON STREAM. ALTHOUGH THE GON IS IN THE PROCESS OF DEVELOPING ADDITIONAL POWER SOURCES THROUGH VARIOUS GEOTHERMAL AND HYDROELECTRIAL PROJECTS, ENERGY FROM THESE SOURCES MAY NOT BECOME AVAILABLE FOR TWO YEARS OR SO.

6. SUMMARY COMMENT: IN THE AGGREGATE VIEW, NICARAGUA OFFERS TO DIRECT INVESTORS A VERY FAVORABLE LEGAL STRUCTURE, LABOR, AVAILABILITY, A TRADITION OF FOREIGN INVESTMENT, AND A GENERALLY PRO-AMERICAN BUSINESS ATMOSPHERE. THERE ARE NUMEROUS SECTORS OF THE NICARAGUAN ECONOMY WHICH OFFER PROMISING OPPORTUNITIES FOR THE FOREIGN INVESTOR. HOWEVER, BUSINESSMEN CONTEMPLATING INVESTMENT IN NICARAGUA ARE URGED TO EXERCISE PRUDENCE AND TO INVESTIGATE THOROUGHLY THE ECONOMIC AND POLITICAL CLIMATE BEFORE MAKING A FINAL DECISION.

7. COPIES OF PERTINENT LAWS TO BE POUCHEO.

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